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Director

# Montana Department of Revenue



Brian Schweitzer  
Governor

SENATE TAXATION

EXHIBIT NO. 10

DATE 4-14-07

FILE NO. HB-644

## Memorandum

TO: Chairman Elliott  
Senate Taxation Committee

FROM: Dan Bucks, Director *Dan Bucks*  
Business and Income Taxes Division Administrator

DATE: April 13, 2007

SUBJECT: House Bill 644 – Additional Fiscal Impact Information

House Bill 644 will require Montana's treatment of net operating losses to conform to the federal provisions for net operating losses. Although administratively this conformity can be accomplished by the department, we still have some concerns regarding the feasibility of tracking and managing net operating losses for up to 20 years.

Also as discussed in the fiscal note, the department is concerned about the long term impact of net operating losses being carried forward for 20 years. The department has gone through a rather lengthy and very manual process of trying to quantify the long term impacts of House Bill 644. The department looked at net operating losses that expired in 2003, 2004 and 2005 due to the current 7 year carry-forward limitation for approximately 40 corporations to try to better quantify the long term impact. If House Bill 644 was the law in effect for tax years 2004 and 2005 these 40 corporations would have paid \$2,295,000 and \$972,000 less in income taxes due to the extension of time allowed for net operating loss carry-forwards for 2004 and 2005 respectively. In addition, these corporations would have had an additional \$12.5 million in "leftover" carryforward losses to continue to use in future years

As stated above the department only had the time to look at 40 corporations. There were approximately 4,500 corporations reporting net operating losses that expired in 2003, 2004 and 2005.

Based on the number of corporations with net operating losses and the detailed information from the 40 corporations, Montana could easily see losses of over \$5,000,000 in corporation tax revenue beginning in FY2016 due to the passage of House Bill 644. The cumulative effect of the carryforward of losses will continue to increase in future years beyond FY 2016.

Please let me know if you have any questions.

**EXPIRED NET OPERATING LOSSES****LARGEST 30-40 NET OPERATING LOSSES REPORTED EACH YEAR**

YEAR	AMT OF NOL EXPIRED DUE TO 7 YR CF LIMIT	TOTAL TAX EFFECT OF EXPIRED NOL
1996 (EXPIRED IN 2003)	104,000,000	7,020,000
1997 (EXPIRED IN 2004)	127,000,000	8,572,500
1998 (EXPIRED IN 2005)	113,000,000	7,627,500
3 YEAR AVERAGE	114,666,667	7,740,000

The above numbers represent the amount of net operating loss that was incurred in the years 1996, 1997, and 1998 that expired in the years 2003, 2004 and 2005, respectively, due to the current 7 year carryforward limitation. This only represents those 30-40 corporations that reported the largest Montana net operating losses for the years 1996, 1997 and 1998. The tax effect could be several million higher if we were to look at all corporations that reported a net operating loss for these years. Approximately 4,500 corporations reported a net operating loss in 1996, 1997 and 1998.

Some of the above corporations did not report income for the years 2003, 2004 or 2005. As such, a large portion of the above tax effect represents amounts that may or may not be claimed by the taxpayer in the future.

The following represents the amount of actual reduction in taxes that would have been paid for these 30-40 corporations on their 2004 and 2005 tax returns had they been allowed to carryforward their net operating losses more than 7 years.

YEAR	AMOUNT OF NOL THAT COULD HAVE BEEN CLAIMED	TAX EFFECT OF ADDITIONAL NOL ALLOWED
2004	34,000,000	2,295,000
2005	14,400,000	972,000
2006	UNKOWN NOT FILED YET	

Had Montana allowed a 20 year carryforward - we would have collected \$2,295,000 less from these 30-40 corporations on their 2004 Montana return and \$970,000 less on their 2005 Montana returns.